

Market Monitor – Asia ex-Japan

Potential Headwinds from Virus Variant



Major Asian economies see strong rebound in Q2 2021

Most Asian economies saw faster economic growth in Q2 2021, mainly due to the low base of comparison. For example, India saw GDP grow by 20.1% in Q2 2021, while Malaysia and Philippines registered growth of 16.1% and 11.8%, respectively. The three countries’ strong performance in Q2 2021 was mainly boosted by robust rebound in household consumption and investment, as well as accelerated growth in exports amid a gradual reopening of advanced economies.

Looking forward, the recovery of major Asian economies is expected to continue for the rest of 2021, as the ongoing recovery of advanced economies like the US and Europe will support Asia’s exports, while domestic reopening will continue with vaccination progress. Nonetheless, the spread of the Delta variant may pose uncertainties for Asia’s recovery trajectory if the efficacy of existing vaccines is seriously reduced. The 7-day average of newly confirmed Covid-19 cases surged to over 270,000 in mid-August. Although the number had declined to about 146,000 as of the end of September, it was still above the level at the end of June. Some Asian economies like Singapore and South Korea have still seen no clear downward trend in newly confirmed cases. If the newly confirmed cases in Asian economies surge again, governments may need to re-impose more stringent mobility restrictions to curb the spread of the virus, which will have a negative impact on business sentiment and household consumption.

More US Federal Reserve officials expect earlier rate hike, which may prompt Asia’s central banks to consider winding down policy support

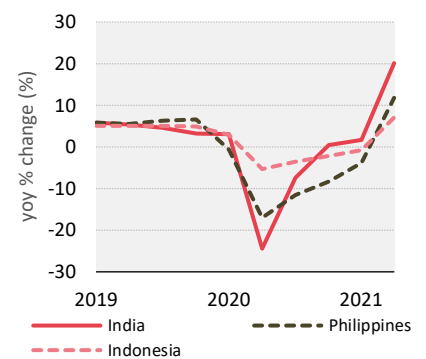
South Korea’s inflation rate stayed at a 9-year peak of 2.6% in August. At its August meeting, the Bank of Korea (BOK) raised the benchmark interest rate by 25 basis points

Spread of Delta variant may pose uncertainties for Asia’s ongoing economic recovery.

Central banks may consider starting to normalise policy support amid elevated inflation and rising financial risks.

Financial markets are being impacted by the course of the pandemic and central bank policies.

GDP of selected Asian economies



Economic Research

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from a record low to 0.75%, making South Korea the first major Asian economy to raise interest rates. The BOK's governor indicated that the rate hike was intended to curb borrowing used for investments in real estate, equities, and other assets amid signs of demand-side inflationary pressures. In Q2 2021, household debt in South Korea rose to a record high of 1.806 quadrillion won (USD1.54 trillion), about 12.1% higher than the level in Q1 2020 when the Covid-19 epidemic was not yet serious in Korea.

More officials of the US Federal Reserve (Fed) were leaning towards an interest rate hike as early as in 2022 at the latest Fed meeting in September compared to at the June meeting. Looking ahead, potential interest rate normalisation earlier than market expectation may result in fund outflows from Asian markets, which central banks in major Asian economies may need to curb by normalising their interest rates. Higher borrowing costs will in turn have an adverse impact on household consumption and business confidence, resulting in slower economic growth in the longer run.

Pandemic developments and central bank policies impact financial markets

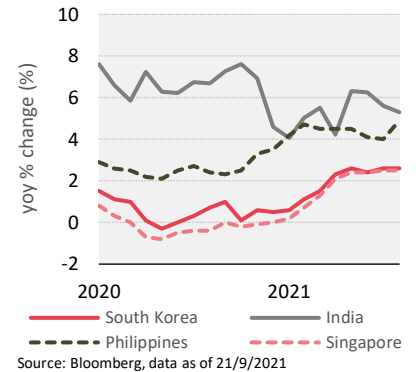
Investor sentiment was adversely impacted in the third quarter of 2021 by a resurgence of confirmed Covid-19 cases, by China's imposition of stricter regulatory requirements on its education and tech sectors, and by concerns about risk in the property sector. As of the end of September, the MSCI Asia ex-Japan index had dropped 9.9% from the level at the end of June, compared to a 3.0% increase in the second quarter. Meanwhile, as the Fed is expected to announce the tapering off of asset purchases as soon as its next meeting, US dollar strengthened. Against this backdrop, most major Asian countries and regions saw their currencies weakened against US dollar by 0.2% to 5.3% in Q3 2021, when compared to the level as of the end of Q2 2021. Nonetheless, Indonesian rupiah and Indian rupee strengthened by 1.3% and 0.1%, respectively, over the same horizon. Meanwhile, Taiwanese dollar remained stable during the quarter.

South Korea saw newly confirmed Covid-19 cases continue to rise in September, while investors were also concerned that memory-chip prices may have peaked. This resulted in a sell-off in Korean semiconductor stocks by global investors, giving the Korean stock market the worst performance among major Asian markets. As of 30th September, South Korea's benchmark equity index had declined by 6.9% from the level at the end of Q2 2021.

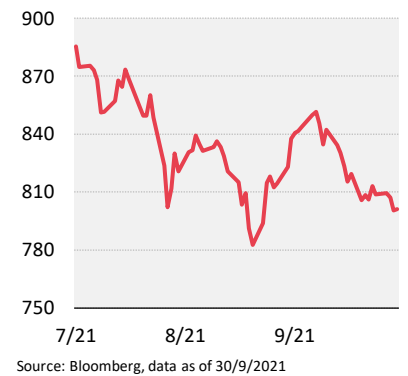
Meanwhile, India's equity market registered a gain of 12.1% and Indonesia's gained 5.0%. India's equity market rally was mainly liquidity-driven, as the Reserve Bank of India has maintained an ultra-easy monetary policy since the start of the pandemic, while Indonesia's stock market performance in current quarter was mainly supported by inflow of foreign investors.

Going forward, the development of the pandemic will continue to impact investor sentiment in the Asian markets. Liquidity in the region will also play an important role in the valuation of the asset markets. When central banks in advanced economies and in Asia start to normalise their monetary policies, elevated asset valuations stemming from low interest rates and ample liquidity may face the risk of correction.

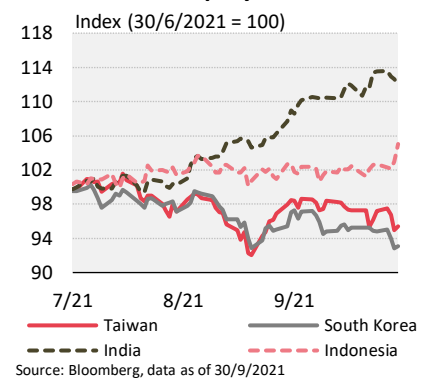
CPI of selected Asian economies



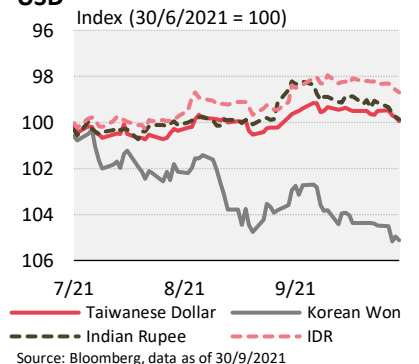
MSCI AC Asia ex Japan Index



Selected Asian equity indices



Selected Asian currencies against USD



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